

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA



FILED
7-28-15
04:59 PM

In the Matter of the Application of SAN JOSE WATER COMPANY (U168W) for an Order authorizing it to increase rates charged for water service by \$34,928,000 or 12.22% in 2016, by \$9,954,000 or 3.11% in 2017, and by \$17,567,000 or 5.36% in 2018.

Application 15-01-002
(Filed January 5, 2015)

**OFFICE OF RATEPAYERS ADVOCATES
REPLY BRIEF REGARDING CONTESTED ISSUES**

I. INTRODUCTION

Pursuant to Rule 13.11 of the California Public Utilities Commission (“Commission”)’s Rules of Practice and Procedure (“Rules”) and pursuant to Commissioner Randolph’s Scoping Memo issued April 14, 2015, the Office of Ratepayer Advocates (“ORA”) submits this reply brief regarding contested issues in this General Rate Case (“GRC”).

While not exhaustive, this brief will focus on some of the arguments raised by San Jose Water Company (“SJWC”) and the Mutual Water Companies (“MWCs”) in their opening briefs.

II. SJWC

A. Revenue Decoupling – WRAM/MCBA

SJWC has not justified its request for a full revenue decoupling Water Revenue Adjustment Mechanism/Modified Cost Balancing Account (“WRAM/MCBA”). SJWC’s opening brief relies on distortion to attempt to argue for WRAM/MCBA, like its statement that “[i]n other words, it is unnecessary for SJWC to promote conservation.”¹

¹ SJWC’s Opening Brief, at 17.

ORA supports water conservation, and in fact supported SJWC's ordinary water conservation programs in this GRC. SJWC and its customers have admirably decreased per capita and total water usage.² These decreases occurred without the proposed full revenue decoupling WRAM/MCBA. SJWC makes a theoretical argument that it would do a better job of conserving water if it had the proposed WRAM/MCBA. But data does not support SJWC's argument. This proposal is not really about conservation, which is happening without the WRAM/MCBA – it is about “revenue protection.”³

B. WRAM - Related Conservation Programs

SJWC attempts to hold the Commission over a barrel on WRAM/MCBA by proposing a series of “WRAM-related conservation programs.”⁴ SJWC's brief on this issue makes an astounding claim:

SJWC . . . challeng[ed] ORA's assertion that SJWC does not need additional conservation programs because it is already meeting its gallons per capita per day targets for 2015 and 2020 pursuant to SB7x-7. [Mr. Pink] noted that ORA's water use charts were incorrect, and that the actual data show that water use can fluctuate . . .⁵

ORA's witness acknowledged that the chart in exhibit O-01 at page 2-14 was incorrect, but that the correct chart appears in exhibit O-01 at page 13-14. To be clear, the correct per capita water usage chart does, in fact, show that SJWC has already met its 2015 and 2020 targets pursuant to SB7x-7.⁶

Mr. Pink believes that the SB7x-7 targets are irrelevant.⁷ Notwithstanding Mr. Pink's opinion, these targets remain highly relevant because the governor's drought

² Hearing Tr. at p. 331:20-332:4; 332:25-333:11.

³ SJWC's Opening Brief at p. 20.

⁴ SJWC's Opening Brief at p. 22.

⁵ SJWC's Opening Brief at p. 23.

⁶ O-01 at p. 13-14.

⁷ Hearing Tr. at p. 307:15-28.

order is scheduled to end at the beginning of this GRC's test year, in February 2016.⁸ SJWC is unwilling to carry out these programs, with one exception, unless it receives its WRAM/MCBA request.² And SJWC's witness, Mr. Pink, considers these long-term programs that "depending on when they are implemented, they may be able to address the short-term drought."¹⁰ Like SJWC's WRAM/MCBA request, this request is not really related to the drought.

As for the one exception that SJWC claims it would carry out without the WRAM/MCBA, that program was funded in rates for three years, but only implemented for about half a year.¹¹ If the company wishes to continue that program, it can use the remaining two and a half years of funding from the last GRC.

C. Labor & Payroll

Escalation factors and methodology

SJWC's opening brief includes a heading that, at best, distorts the company's escalation methodology. In the heading, the company states, "SJWC based its forecast on actual salaries paid in 2015 and realistic escalation rates."¹² 2015 is a little over halfway complete. As of the filing of these briefs, there are no actual recorded salaries for 2015. That was also true when SJWC filed its application in January of 2015.

SJWC asserts that the Energy Cost of Service ("ECOS") labor factor is "anomalous,"¹³ but it uses the ECOS factors abundantly in this proceeding, including in escalating payroll in 2017 and 2018.¹⁴ The only "anomalous" labor factor at issue in this case is the 5% factor Ms. Leal proposed. While SJWC's brief alludes to Ms. Leal's

⁸ Hearing Tr. at p. 343:5-10.

² Hearing Tr. at p. 309:19-310:19.

¹⁰ Hearing Tr. at p. 309:2-18.

¹¹ ORA's Opening Brief at p. 3-4.

¹² SJWC's Opening Brief at p. 25.

¹³ SJWC's Opening Brief at p. 26.

¹⁴ E.g., SJWC's Opening Brief at 26 (The Company then used the PUC-published forecasts to escalate to 2017 and 2018.)

assertion that the Bureau of Labor Statistics (“BLS”) has a different labor inflation factor than ECOS, the company declines to mention that the BLS factor is less than half of the factor Ms. Leal proposes.¹⁵

SJWC’s asserts that a news article and a BLS release about wages and salaries, generally, in the Bay Area—not wages and salaries of utility employees – demonstrate that the ECOS escalation factor is too low.¹⁶ Yet SJWC uses ECOS for 2017 and 2018 payroll escalation. And the company uses an anomalous 5% factor for administrative employees and officers in 2016.

The best approach to escalation is ORA’s – using actual recorded payroll escalated using ECOS factors.

New Positions

SJWC erroneously states that “ORA would allow only two new positions” in this GRC.¹⁷ ORA proposes allowing five new positions in rates.¹⁸ SJWC ignores its own use of utility employees for Non-Tariffed Products and Services (“NTP&S”), which increases the burden on utility labor by decreasing the number of employee hours available to conduct utility operations. Rather than increasing rates to fund 33 new positions when customers are being asked to cut back on water and the equivalent of 6 full-time employees are being utilized to provide *unregulated* services under alleged “excess capacity,”¹⁹ SJWC should use the positions that have already been funded more efficiently (including filling of the 15 funded but vacant positions) in order to provide *regulated* utility services.

¹⁵ 2.4% rather than 5%, SJWC’s Opening Brief at 27-28, Hearing Tr. at p. 390:14-20.

¹⁶ SJWC’s Opening Brief at p. 28.

¹⁷ SJWC’s Opening Brief at p. 29.

¹⁸ O-01 at p. 3-12:5-6.

¹⁹ O-01 at p. 3-3:13-14.

Temporary and Part-Time Positions

SJWC asserts that its union contracts allow temporary labor “to provide relief during peak summer months.”²⁰ It did not establish that union contracts *require* the company to use temporary labor. Like the last GRC, temporary and part-time labor expenses should be excluded from the revenue requirement.²¹

Bonuses for Officers and Managers

SJWC ignores the fact that its incentive plans focus on shareholder benefits. The company has not established any ratepayer benefits that justify including these costs in rates. In fact, the company admits that the company’s long-term incentive plan “responds to concerns of shareholder advocates that a significant portion of officer compensation should be aligned with shareholders’ interests.”²² The plan is not a ratepayer benefit – it is a shareholder benefit.

SJWC is correct that the opportunity to earn bonuses for officers, managers, and supervisors is “consistent with standard principles of good corporate governance.”²³ But without a showing that such bonuses are necessary to provide safe and reliable water service, SJWC seems content with pointing out the shareholder benefits from the bonus programs. While the company’s management and shareholders may think those shareholder benefits are an appropriate goal of conducting business, they should not be funded by ratepayers in rates absent a commensurate benefit to ratepayers.

Overtime

SJWC does not justify using a smaller sample of data – a 3-year average – to forecast overtime expenses. A 5-year average, as ORA uses, does a better job of

²⁰ SJWC’s Opening Brief at p. 33.

²¹ SJWC’s Opening Brief at p. 33.

²² SJWC’s Opening Brief at p. 37-38.

²³ SJWC’s Opening Brief at p. 38.

smoothing abnormally high or low expense years, like the abnormally high overtime year of 2013.²⁴

NTP&S Payroll

SJWC ignores its obligation to prove that its NTP&S are being offered consistent with the NTP&S rules under D.10-10-019.²⁵ In this GRC, SJWC asserts that it needs 33 new employees in the revenue requirement, presumably for its regulated business. Yet it continues to use labor for its regulated business to provide NTP&S. The company has never explained how it has excess labor capacity to provide NTP&S, yet it needs to hire 33 new employees. It is simply illogical to assume the company has excess labor capacity when many of the new positions it requests in this GRC are the same as those positions it uses for NTP&S as excess capacity.²⁶ That is the precise excess capacity concern raised in D.15-03-048.

D. Regulatory Commission Expense

SJWC fails to recognize that a 5-year, inflation-adjusted average captures cost variation throughout a three-year cycle Rate Case Plan.²⁷ SJWC's forecast is essentially a number plucked from thin air--\$1 million over 2016, 2017, and 2018.²⁸ In its opening brief, SJWC modifies ORA's method to use a 6-year base period, which increases ORA's forecast from \$185,000 in 2016 to a calculated \$216,000 in 2016.²⁹ But even this 6-year average is far less than SJWC's actual forecast in this GRC--\$341,000 in 2016.³⁰ In fact, it is much closer to ORA's forecast than it is to SJWC's.

²⁴ O-01 at p. 3-12:14-20.

²⁵ D.15-03-048 at p. 6-7 ("If the labor associated with providing NTP&S is needed by the regulated business, it raises the issue of whether SJWC should be using the labor to provide NTP&S and whether SJWC is in compliance with our NTP&S' rules.")

²⁶ O-01 at p. 3-11:13-16.

²⁷ SJWC's Opening Brief at p. 44.

²⁸ O-01 at p. 2-29:1.

²⁹ SJWC's Opening Brief at p. 44.

³⁰ O-01 at p. 2-28:20-23.

SJWC also fails to recognize that ORA’s forecast actually does capture costs associated with SJWC’s last Cost of Capital application – it is a 5-year average, not a 3-year average.³¹

E. Corporate Expense

Costs fluctuate in this category, so a 5-year, inflation-adjusted forecast is appropriate; there is not an “upward trend” justifying SJWC’s forecast.³²

F. Payroll Taxes – Capitalized Portion of FICA Tax

Capitalized payroll should be removed from payroll taxes and added back into administrative expenses transferred to reflect actual payroll taxes.³³ A history of using flawed forecasting methodology does not justify using a flawed approach in this proceeding.³⁴

G. Tax Memorandum Accounts

SJWC’s argument against both the Tangible Property Regulation (“TPR”) and the California Enterprise Zone Sales and Use Tax Credit (“EZ Credit”) memorandum accounts is that the accounts would constitute unjustified retroactive ratemaking.³⁵ This argument should be ignored because SJWC has yet to file its tax year 2014 federal taxes, which will be the tax filing in which SJWC reclassifies capital expenditures dating back to 2006.³⁶ Logic determines that a ratemaking mechanism impacting a future tax filing is by definition not retroactive ratemaking. SJWC simply ignores the key point: the TPR tax law change is before the Commission now, before SJWC has filed for expense reclassification, and therefore the actual tax expenditure is ongoing now (or yet to come, really). Therefore, there is no retroactive ratemaking concern.

³¹ See ORA’s Opening Brief at p. 13.

³² O-01 at p. 2-30:8-12.

³³ See ORA’s Opening Brief at 14, SJWC’s Opening Brief at p. 48.

³⁴ SJWC’s Opening Brief at p. 48.

³⁵ SJWC’s Opening Brief at p. 48.

³⁶ Hearing Tr. at p. 292:4-294:16.

Additionally, the Commission has a history of treating tax law changes as the type of expense change that warrants memorandum account treatment.³⁷ And such memorandum accounts have not been considered retroactive ratemaking; in fact, they are a method to avoid retroactive ratemaking: “This mechanism [a one-way memorandum account to track the impacts of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010] simply allows the Commission to determine at a future date whether rates should be changed, without having to be concerned with issues of retroactive ratemaking.”³⁸

Relatedly, SJWC argues that a memorandum account cannot be used to “adjust rates for costs or benefits accruing prior to authorization of the accounts.”³⁹ For this assertion, SJWC cites to a 1992 Commission Decision that declined to provide a utility with rate recovery for ownership costs associated with a new general office while the company was still occupying its old general office.⁴⁰ In other words, the Commission only allowed the company to recover costs for one general office in rates even though the company simultaneously incurred costs for two general offices. Of course, the utility had considerable control over its disposition of the general offices, and had ample opportunity to request ratemaking treatment that would allow rate recovery for those costs.

Here, the tax law change is outside the utility’s control and outside of ratepayer control. Because the tax law change allows SJWC to reduce its past taxes with a future filing, the company does not have an interest in “avail[ing] itself of the regulatory procedures available in this regard”⁴¹ to accurately reflect expenditures and pass tax savings along to ratepayers. Without ORA’s proposed memorandum account, when SJWC files its taxes in September, it will receive a significant windfall in tax savings –

³⁷ See, e.g., Res. L-411 (admitted as O-02) at p. 1.

³⁸ Res. L-411 at p. 1-2.

³⁹ SJWC Opening Brief, at p. 3.

⁴⁰ D.92-03-094, 1992 Cal PUC Lexis 236 at p. *7.

⁴¹ *Id.* at p. 9.

from taxes that ratepayers have already been paying in rates for nearly a decade. Failing to require the memorandum account would be a fundamentally unfair approach to ratemaking and the Commission should rectify the problem by authorizing the memorandum accounts ORA proposes. The Commission cannot rely on utilities to file applications between GRCs for memorandum accounts that will return unanticipated tax savings to ratepayers.

H. Health Care Cost Balancing Account

SJWC fails to recognize that a balancing account for health care costs would remove incentives to achieve cost savings in health care benefits.⁴² For that reason alone, the company's proposal is flawed.

III. MUTUALS

While ORA generally has no position on the issues raised by the MWCs, one issue that the MWCs repeatedly raise in their opening brief requires response. The MWCs assert that SJWC under-collects "costs of service" from residential customers while "over-collecting" costs from other customer classes, including the MWCs themselves.⁴³ This claim is unsubstantiated. As Mr. Burke acknowledged at hearing, the data from SJWC's workpapers shows that residential customers used about 58.4% of the water sold by SJWC and they paid about 62.4% percent of the total revenues.⁴⁴ By contrast, using the numbers evaluated in the MWCs' testimony,⁴⁵ resale customers – a category that includes MWCs, used about 0.7% of the water sold by SJWC,⁴⁶ but paid only about 0.5%

⁴² ORA's Opening Brief at p. 17.

⁴³ See, e.g., MWCs' Opening Brief at 2, 28 ("SJWC has Advantaged the Residential Customer Class from the huge under-collection of rate of Return dollars").

⁴⁴ Hearing Tr. at pgs. 282:2-21; 282:22-283:17; 283:18-22.

⁴⁵ M-1, at p. 33 (alternatively, Attachment 7 to M-1)

⁴⁶ 398,500 CCF total resale / 53,332,200 CCF grand total 2015.

of the total revenues.⁴⁷ Total revenues and quantity usage make clear that residential customers are paying their fair share for water service.

That would not be true under the MWCs' proposed rate design, in which residential customers, using 2015 numbers, would pay more than 90.0% of total revenues⁴⁸ while using only about 58.4% of the water sold by SJWC. But MWCs' proposed rate design would have resale customers, like the MWCs themselves, pay 0.0149% of total revenues⁴⁹ while using 0.7% of the total water sold.

IV. CONCLUSION

For the foregoing reasons, ORA respectfully requests that the Commission adopt ORA's recommendations on the contested issues.

Respectfully Submitted,

/s/ JOHN R. REYNOLDS
JOHN R. REYNOLDS

Attorney for
The Office of Ratepayer Advocates

California Public Utilities Commission
505 Van Ness Avenue
San Francisco, California 94102
Telephone: (415) 703-1642
Facsimile: (415) 703-4432
E-Mail: Jr5@cpuc.ca.gov

July 28, 2015

⁴⁷ \$1,581,330 total resale revenue / \$281,801,753 grand total 2015 revenue.

⁴⁸ Attachment 7 to M-1, at Tab 2 (\$253,682,064 total residential revenue / \$281,801,000 grand total revenue)

⁴⁹ Attachment 7 to M-1, at Tab 2 (\$42,138 total resale revenue / \$281,801,000 grand total revenue).